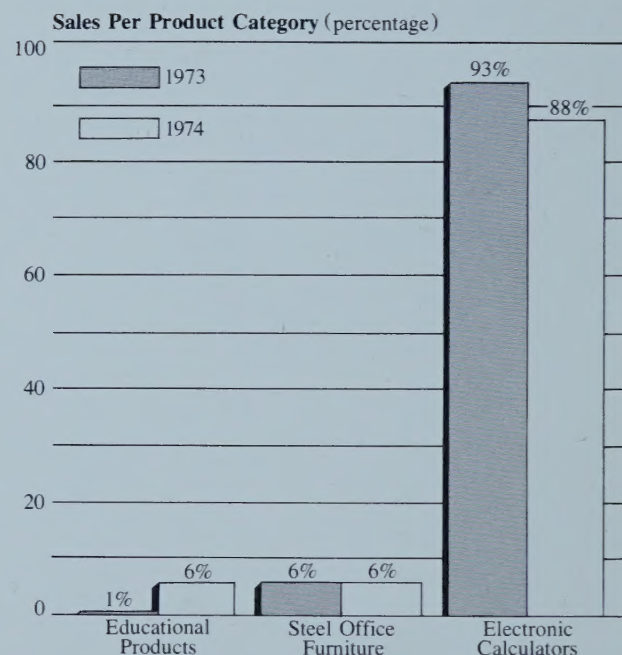
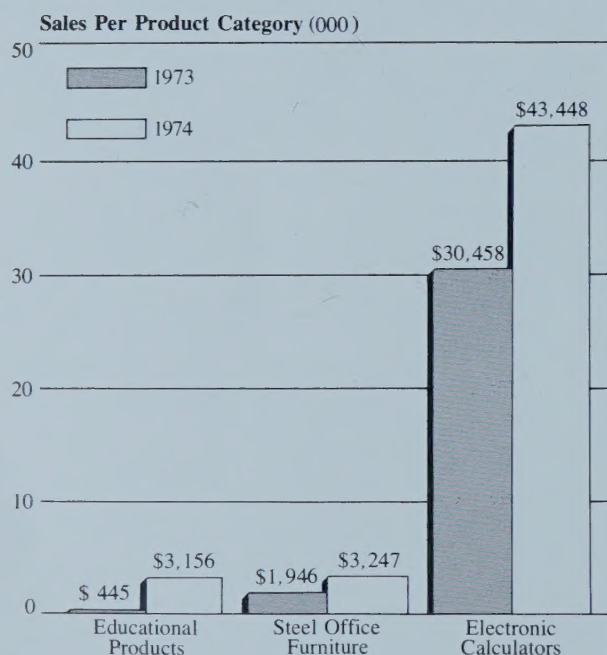


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Commodore Business Machines Annual Report 1974



7 Year Financial Highlights

(United States Currency)	1974	1973	1972	1971	1970	1969	1968
SALES	\$49,850,924	\$32,848,680	\$22,151,844	\$13,494,272	\$9,418,321	\$7,477,426	\$4,139,886
EARNINGS (before extraordinary items)	\$ 445,883	\$ 2,288,321	\$ 1,361,624	\$ (275,065)	\$ 695,310	\$ 467,476	\$ 130,750
EARNINGS PER SHARE (before extraordinary items based on Canadian Method)	\$.35	\$ 1.83	\$ 1.11	\$ (.23)	\$.58	\$.41	\$.12
SHARES OUTSTANDING (average number)	1,268,110	1,252,535	1,229,333	1,215,615	1,197,487	1,146,241	1,094,987
WORKING CAPITAL	\$ 6,812,696	\$ 6,728,882	\$ 4,341,065	\$ 3,013,625	\$3,379,449	\$2,480,096	\$1,725,175
SHAREHOLDERS' EQUITY	\$ 8,916,307	\$ 8,461,741	\$ 5,227,359	\$ 3,315,327	\$3,613,362	\$2,785,036	\$1,962,457

To the Shareholders:

In many ways fiscal 1974 was a successful year; it was a year of growth, transition and expansion for Commodore. Sales reached record heights, increasing by 52% over the previous year. But in one way, it was not: We are reporting appreciably reduced profits for the fiscal year.

Sales for the twelve months ended June 30, 1974, reached \$49,851,000 as compared to \$32,849,000 during the previous fiscal period. Net earnings before extraordinary item was \$446,000 for the current year, compared to \$2,288,000 at the close of fiscal 1973.

ACCOUNTING POLICIES

Our accounting policies have been applied in our 1974 report in the light of current economic and business conditions. We have taken major write-downs in our inventories of finished goods and of raw materials. We have also considered the current business climate in evaluating the deferral of the costs of our research and development efforts. Most of the research and development incurred in 1974 was expensed in addition to amortizing a substantial portion of the amount deferred at June 30, 1973, increasing our reported expenditure from \$212,000 in the year previous to \$1,165,000 this year. Also, we have increased our reserves for customer returns, bad debts and service liabilities. We believe these steps will give us a more solid base upon which to enter the new year.

OPERATING EXPENSES

Selling Expenses	1974	1973
Calculators and Furniture	\$1,969,000	\$1,158,000
Educational Products	1,341,000	263,000
Total	<u>\$3,310,000</u>	<u>\$1,421,000</u>

The increase in selling expenses related to calculators and furniture results primarily from two factors. A manufacturer's representative organization on a commission basis was established in 1974. In addition, the Company's own world-wide sales force was increased. Costs (principally commissions) for educational products varies almost directly with sales volume, which increased from \$445,000 in the three months of operations in 1973 to \$3,156,000 for 1974, the first full year of operations.

General and Administrative	1974	1973
Calculators and Furniture	\$2,094,000	\$1,348,000
Educational Products	759,000	102,000
Total	<u>\$2,853,000</u>	<u>\$1,450,000</u>

General and Administrative costs are generally related to the substantial increases in sales and the corresponding strengthening of related staffs to keep pace with the growth. The change in operation from 1972 when most electronic calculators were purchased as completed machines, to the in-house procurement of component parts and assembly by the end of 1974, required considerably more depth in all support functions. Included in 1974 are costs related to the company's application and listing on the American Stock Exchange in May, 1974, and the corresponding Security and Exchange Commission filings.

Interest Expense (Income)	1974	1973
Calculators and Furniture	\$907,000	\$260,000
Educational Products	64,000	(9,000)
Total	<u>\$971,000</u>	<u>\$251,000</u>

In addition to the overall increase in business activity, the higher interest expense is the direct result of two particular items. The change to in-house procurement and assembly of component parts, referred to above, required substantial increases in raw material and work-in-process inventories over the last 18 months. Fiscal 1974 reflects the first full year of the related borrowing costs. Also, interest rates were at a higher level throughout the current year.

Conditional sales contracts for educational products include fixed interest charges related to the rate prevailing at the date of sale, but the company's loans fluctuate with changes in the prime rate. Therefore, the interest costs exceeded interest income.

ADJUSTMENTS IN THE FOURTH QUARTER

Sales during the three months ended June 30, 1974 were approximately \$13,300,000. However, a change in the method of recognizing certain sales and costs of sales was made in the fourth quarter; if the change had been made as of March 31, 1974, sales for the nine months would have been reduced by approximately \$5,100,000 with no significant effect upon gross profit. These sales were made to a third party because of import license restrictions. A Commodore subsidiary then repurchased the same components for assembly of electronic calculators.

During the fourth quarter of fiscal 1974, the availability of components and the economic situation caused production in the industry to outstrip demand for the first time, which resulted in sales price decreases in advance of continuing cost reductions. This change from a "sellers' market" to a "buyers' market" had a significant effect, not only on Commodore, but on the entire industry. In recognition of lower selling prices and a more liberal return-of-product policy to the Company's customers, the results of operations in the fourth quarter were adversely affected by year-end adjustments totalling \$2,900,000 (before tax effect), primarily related to inventory write-downs and accounts receivable credits.

FACTORS FOR GROWTH

Our continued investment in research and technology has resulted in excellent progress in the development of our own integrated circuits. This capability, coupled with our policy of going to outside sources whenever feasible, has proved, once again, to be an essential formula for our planned growth.

A major change toward complete manufacturing independence is another significant step in our progress. New plants were opened in Palo Alto, California; Eaglescliff, England; and Bristol, Virginia. Today, these assembly locations account for almost 90% of our total production.

In May, 1974, Commodore was listed on the American Stock Exchange.

Our private label business showed a measurable increase during the past year. We believe this to be a vital part of our future marketing activity and anticipate an even greater share of this business next year.

LOOKING AHEAD

What does fiscal year 1975 hold for us? We are prepared to assume the possibility of continuing tight money and an economy that will reflect a decreasing rate of growth. We expect to increase our share of the market in each of our product lines because we have consistently demonstrated the ability to design products that offer greater values to the consumer at competitive prices. In the face of increasing price competition, we feel we have the knowledge and the market penetration to sell more of our products than ever before.

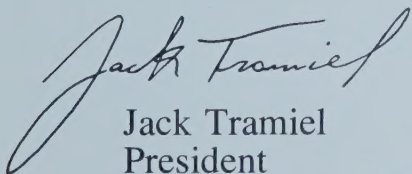
At the same time, we are prepared to put on the shelf temporarily several products which are now in the planning stage and which would require major capital investment. We will report new product developments as the economy, technology and availability of money dictate.

Fiscal 1975 will be a year of consolidation, of taking a realistic look at the money supply and the economy . . . of pledging our efforts to greater efficiency, to a better return on investment and to making our company more viable and profitable.

A CLOSING NOTE

In closing, let me say that the progress we have achieved during the past year can be measured in terms of people. To our employees, our suppliers, our customers, our shareholders and our many international business associates, I join with my fellow directors in extending our sincere appreciation.

It is our hope that we may continue to enjoy the support of each of you.



Jack Tramiel
President

September 30, 1974

Commodore Business Machines (Canada) Limited and Subsidiaries Consolidated Balance Sheets

(Expressed in United States Currency)

	June 30,	
	1974	1973
ASSETS		
Current Assets:		
Cash, including short-term deposits of \$112,327 in 1974 and \$20,000 in 1973	\$ 522,570	\$ 1,400,098
Deposits pledged as security for letters of credit and as compensating balances (Note 7)	582,999	—
Trade receivables, less allowance of \$632,911 in 1974 and \$606,741 in 1973 for doubtful accounts (Notes 4 and 7)	8,238,703	6,446,872
Income taxes recoverable	100,000	132,137
Receivable from a joint venture	109,920	—
Advances to suppliers	284,327	—
Inventories, at the lower of cost (first-in, first-out) or market (Notes 1 and 7)-		
Finished goods	6,574,425	3,369,121
Raw materials and work-in-process	11,975,460	11,322,691
Prepaid expenses	171,337	178,710
Total current assets	28,559,741	22,849,629
Property and Equipment , at cost (Notes 1 and 7)	2,624,229	1,209,779
Less-Accumulated depreciation and amortization	900,283	514,631
	1,723,946	695,148
Other Assets:		
Investments (Notes 1 and 3)	64,666	60,700
Deferred product development and preoperating costs of a subsidiary (Note 4)	813,100	844,047
Research and development costs (Notes 1 and 5)	562,366	1,044,229
Lease deposits and other assets	266,242	139,479
Patents, trademarks and other manufacturing rights	1	1
	1,706,375	2,088,456
	<u>\$31,990,062</u>	<u>\$25,633,233</u>

Approved on behalf of the Board;
Irving Gould, Director
Jack Tramiel, Director

The accompanying notes to consolidated financial statements are an integral part of these consolidated balance sheets.

	June 30,	
	1974	1973
LIABILITIES		
Current Liabilities:		
Bank overdrafts	\$ 233,692	\$ —
Advances from finance company, secured by certain receivables and inventories (Note 7)	5,054,447	4,164,846
Notes payable to banks and others (Note 7)	3,119,207	2,347,884
Drafts payable	3,245,083	1,403,025
Accounts payable	8,440,426	6,928,694
Accrued liabilities	1,235,591	649,196
Income taxes payable	418,599	627,102
Total current liabilities	21,747,045	16,120,747
Deferred Income Taxes	207,756	510,000
8½% Mortgage Payable (Note 7)	601,472	—
Minority Interest in a Subsidiary (Note 4)	517,482	540,745
Commitments and Contingent Liabilities (Notes 9 and 10)		
Shareholders' Equity:		
Capital stock (Note 8)-		
Preferred stock, \$10 par value; authorized 100,000 shares, none outstanding	—	—
Common stock, no par value;		
Authorized—3,000,000 shares;		
Outstanding—1,269,818 shares in 1974 and 1,259,318 shares in 1973	2,012,479	1,977,229
Retained earnings	6,022,392	5,576,509
Contributed surplus	881,436	908,003
	8,916,307	8,461,741
	<u>\$31,990,062</u>	<u>\$25,633,233</u>

Commodore Business Machines (Canada) Limited and Subsidiaries

Consolidated Statements of Operations

(Expressed in United States Currency)

	Year Ended June 30,	
	1974	1973
Net Sales (Note 1).....	\$49,850,924	\$32,848,680
Cost of Sales	41,032,162	25,953,514
Gross profit	8,818,762	6,895,166
Operating Expenses:		
Selling	3,309,938	1,420,534
General and administrative	2,853,099	1,450,401
Research and development (Note 1).....	1,164,795	212,319
Interest expense, net of interest income of \$165,200 in 1974 and \$66,400 in 1973	970,047	250,591
	8,297,879	3,333,845
Income from operations	520,883	3,561,321
Provision (Credit) for Income Taxes (Notes 1 and 2):		
Current	377,244	763,000
Deferred	(302,244)	510,000
	75,000	1,273,000
Income before extraordinary item	445,883	2,288,321
Extraordinary Item—		
Reduction of income taxes resulting from carryforward of prior years' losses	—	192,000
Net income	\$ 445,883	\$ 2,480,321

	1974		1973	
Earnings Per Share (Note 11):	Income Before Extraordinary Item	Net Income	Income Before Extraordinary Item	Net Income
Canadian Method—				
Primary	\$.35	\$.35	\$1.83	\$1.98
Fully diluted35	.35	1.45	1.56
United States Method—				
Primary	\$.33	\$.33	\$1.51	\$1.64
Fully diluted33	.33	1.51	1.64

The accompanying notes to consolidated financial statements are an integral part of these statements.

Commodore Business Machines (Canada) Limited and Subsidiaries

Consolidated Statements of Changes in Financial Position

(Expressed in United States Currency)

	Year Ended June 30,	
	<u>1974</u>	<u>1973</u>
Funds Were Provided By (Used For):		
Operations, exclusive of extraordinary item-		
Income before extraordinary item	\$ 445,883	\$2,288,321
Items not requiring outlay of working capital in the current period-		
Depreciation and amortization (Substantially straight-line)	1,283,346	449,366
Write-down of investments	19,334	—
Increase (decrease) in deferred income taxes	(302,244)	510,000
Minority interest in loss of a subsidiary	(23,263)	—
Total provided by operations	1,423,056	3,247,687
Extraordinary item	—	192,000
	1,423,056	3,439,687
Sale of common stock	35,250	72,838
Net proceeds from public offering by majority-owned subsidiary	(26,567)	1,221,968
Mortgage payable on purchase of building	615,000	—
	2,046,739	4,734,493
Funds Were Applied To:		
Mortgage payments	13,528	—
Purchase of equipment, building and improvements	1,475,901	631,605
Expenditures for-		
Deferred product development and preoperating costs of a subsidiary	151,470	552,116
Research and development costs	171,963	1,017,476
Investments	23,300	6,000
Other assets	126,763	139,479
	1,962,925	2,346,676
Increase in working capital	\$ 83,814	\$2,387,817
Changes In Components Of Working Capital:		
Increase (decrease) in current assets-		
Cash, short-term deposits and marketable securities	\$ (877,528)	\$(1,037,150)
Deposits pledged	582,999	—
Receivables and advances to suppliers	2,186,078	3,767,071
Income taxes recoverable	(32,137)	58,137
Inventories	3,858,073	12,949,631
Prepaid expenses	(7,373)	22,346
(Increase) decrease in current liabilities-		
Advances from finance company	(889,601)	(4,164,846)
Notes payable and bank overdrafts	(1,005,015)	(1,847,884)
Accounts and drafts payable and accrued liabilities	(3,940,185)	(6,979,962)
Income taxes payable	208,503	(379,526)
Increase in working capital	\$ 83,814	\$2,387,817

The accompanying notes to consolidated financial statements are an integral part of these statements.

Commodore Business Machines (Canada) Limited and Subsidiaries

Consolidated Statements of Shareholders' Equity and Notes to Consolidated Financial Statements

June 30, 1974 (Expressed in United States Currency)

SHAREHOLDERS' EQUITY	Common Stock		Retained Earnings	Contributed Surplus	Total
	Shares	Amount			
Balance, June 30, 1972	1,242,152	\$1,904,391	\$3,096,188	\$226,780	\$5,227,359
Net income for the year			2,480,321		2,480,321
Sale of common stock upon exercise of options and warrants ..	17,166	72,838			72,838
Increase in equity in Commodore Educational Systems Limited resulting from the subsidiary's sale to the public of a minority interest in its stock				681,223	681,223
Balance, June 30, 1973	1,259,318	1,977,229	5,576,509	908,003	8,461,741
Net income for the year			445,883		445,883
Sale of common stock upon exercise of options and warrants ..	10,500	35,250			35,250
Decrease in equity in Commodore Educational Systems Limited resulting from the subsidiary's sale of 10,000 shares to an individual				(26,567)	(26,567)
Balance, June 30, 1974	1,269,818	\$2,012,479	\$6,022,392	\$881,436	\$8,916,307

The accompanying notes to consolidated financial statements are an integral part of these statements.

1. Summary of Accounting Policies

Principles of Consolidation—The consolidated financial statements include the accounts of Commodore Business Machines (Canada) Limited and all subsidiaries after elimination of intercompany accounts and transactions. All such subsidiaries were wholly-owned as of June 30, 1974, except for Commodore Educational Systems Limited in which the Company holds an interest of 61% (see Note 4).

In July, 1973, the Company became a 50 percent owner in Commodore France S.A., a joint venture. The Company's investment in Commodore France, S.A. is accounted for on the equity method. At June 30, 1974, the financial statements carried an investment of \$23,300 and reflected a loss of \$5,634.

The consolidated financial statements are expressed in United States currency. For foreign operations, current assets and current liabilities have been translated at year-end rates of exchange and all other assets and liabilities have been translated at historical rates. Income, costs and expenses were translated at average rates prevailing during the year. Gains or losses resulting from translations are included in the consolidated statements of operations. Such gains and losses have not been material.

Equipment and Improvements—Major classes of equipment and improvements are as follows:

Description	June 30,		Estimated Useful Lives
	1973	1974	
Machinery and equipment	\$ 552,641	\$ 650,107	2-10 years
Building and improvements	—	781,336	25 years
Furniture and fixtures	122,946	332,913	5-10 years
Tooling	461,178	745,344	Expected sales (not to exceed two years)
Leasehold improvements	73,014	114,529	Life of lease
Total	\$1,209,779	\$2,624,229	

Depreciation has been provided using the straight-line method over the estimated useful lives of the assets for both financial reporting and income tax purposes.

Expenditures for maintenance and repairs are charged to expense as incurred. Expenditures for major betterments or renewals are capitalized.

The net gain or loss on items of equipment retired or otherwise disposed of is credited or charged to income and the asset cost and related accumulated depreciation or amortization are removed from the accounts.

Research and Development Costs—Research and development costs incurred in connection with the development of new products are capitalized for book purposes and amortized by charges against income based upon an initial number of expected sales over a period estimated not to exceed three years (see Note 5). Should it be determined in any period that

any deferred costs cannot be recovered from future revenues, they will be written off against operations for that period. Beginning in 1973, research and development costs are deducted for tax purposes in the year incurred, and accordingly, deferred income taxes are provided in the accompanying consolidated financial statements.

Patents, Trademarks and Other Manufacturing Rights—The Company expenses all costs of obtaining patents, trademarks and other manufacturing rights in the year incurred.

Investment Tax Credits—The Company accounts for investment tax credits as a reduction of the provision for taxes on income in the year in which the related credit is utilized. Such credits have not been material.

Reclassifications—Certain reclassifications have been reflected in the consolidated financial statements for the year ended June 30, 1973, to present it on a basis comparable with 1974.

Sales—During fiscal 1974, two customers accounted for 21% of net sales. Also in fiscal 1974, sales included approximately \$1,700,000 to a company which is 80% owned by the Chairman of the Company's Board of Directors. Such sales were at arms length and on terms no more favorable than to other customers.

2. Income Taxes

In prior years, Commodore Business Machines, Inc., a United States subsidiary, filed claims for refund of income taxes paid for fiscal years 1962 to 1964. During fiscal 1970, certain items were settled in the Company's favor. In fiscal 1972, additional settlements were reached. The final refund of \$74,000 (net of certain expenses) plus interest was received in the first quarter of fiscal 1974. The interest received of \$41,200 resulting from these settlements is included in the consolidated statements of operations for 1973.

Income tax expense charged to operating income is made up of the following:

	U.S.		State	
1974	Federal	Foreign	and Local	Total
Current tax expense (credit)	\$ (100,000)	\$451,244	\$ 26,000	\$ 377,244
Deferred tax expense	\$ (302,244)	—	—	(302,244)
Total	\$ (402,244)	\$451,244	\$ 26,000	\$ 75,000
1973				
Current tax expense	\$ 515,551	\$ 82,476	\$164,973	\$ 763,000
Deferred tax expense	510,000	—	—	\$ 510,000
Total	\$1,025,551	\$ 82,476	\$164,973	\$1,273,000

The provision for deferred income taxes results from research and development costs deducted for income tax purposes and capitalized for book purposes in the year incurred.

The provision for income taxes of \$75,000 for 1974 and \$1,273,000 for 1973 represented an effective income tax rate of 14% and 36% respectively. These provisions differ from the amount computed by applying the U.S. Federal income tax rate of 48% to income before tax due principally to:

	1974	% of	1973	% of
	Amount	Income	Amount	Income
Computed "Expected Tax"	\$250,000	48%	\$1,709,000	48%
Foreign income taxes	—	—	33,000	1
Subsidiaries incorporated in a jurisdiction which does not levy income taxes	(497,000)	(95)	(540,000)	(15)
Benefits of losses in Foreign subsidiaries not recognized	304,000	58	—	—
State income taxes, net of Federal income tax benefit	14,000	3	86,000	2
Miscellaneous, net	4,000	—	(15,000)	—
	\$ 75,000	14%	\$1,273,000	36%

3. Investments

During 1973, Commodore Business Machines, Inc. sold its 70 percent interest in Optimized Technology, Inc. In exchange, Commodore received 27,350 shares of capital stock of Standard Microsystems Corporation, and rights to certain product research. These shares are restricted from sale until November, 1974.

The Standard Microsystems Corporation capital stock was purchased by Optimized Technology for \$54,700 in 1972. As a result of the settlement of intercompany advances, product research has been included by the Company at its cost of \$78,270 in research and development costs for 1973 and \$39,135 for 1974 in the accompanying consolidated balance sheet. In fiscal 1974, the investment was written down to market value.

4. Commodore Educational Systems Limited

The Company formed a Bahamian subsidiary, Commodore Educational Systems Limited, to develop, promote and market, initially in Japan, a table-model language laboratory and teaching machine, together with courses for use in conjunction with this machine. The subsidiary was in the development stage until March 31, 1973. Product development and preoperating costs incurred through March 31, 1973 have been deferred and are being amortized based on the total estimated units of sales from March 31, 1973 to June 30, 1976.

An analysis of deferred product development and preoperating costs for the three years ended June 30, 1974, is as follows:

Fiscal Year Ended	Balance at Beginning of Period	Additions at Cost	Deductions Charged to Costs and Expenses	Balance at Close of Period
1972	\$ 41,490	\$258,819	\$ —	\$300,309
1973	300,309	552,116	(8,378)	844,047
1974	844,047	151,470	(182,417)	813,100

The sales of Commodore Educational Systems Limited are primarily made pursuant to conditional sales contracts and are accounted for on the accrual basis. The unearned interest charged to customers on installment sales is reflected in the accompanying consolidated balance sheets as a reduction from accounts receivable. At June 30, 1974, \$1,647,855 of accounts receivable (net of unearned interest of \$85,287) are due in installments including \$434,062 due after one year.

Commodore Educational Systems Limited completed a public offering of 180,000 shares of its capital stock in January 1973 (which resulted in a 38% minority interest). The net proceeds of the offering (approximately \$1,222,000) were used to liquidate \$500,000 of unsecured 7% notes payable, including \$400,000 issued to a Bahamian corporation owned by the Chairman of the Company's Board of Directors, and the balance for working capital purposes. The public offering was for \$9.50 per share which was greater than the Company's per share investment in the subsidiary, thus resulting in contributed surplus to the parent company of \$681,223. During fiscal 1974 an additional 10,000 shares of the subsidiary's capital stock were sold which reduced the parent company's contributed surplus to \$654,656 and increased the minority interest to 39%.

5. Research and Development Costs

As of June 30, 1974, the Company had deferred research and development costs of \$562,366 resulting principally from the development of integrated circuits. The Company amortizes these costs based upon an initial number of expected sales over a period not to exceed three years.

An analysis of Research and Development costs for the three years ended June 30, 1974 is as follows:

Fiscal Year Ended	Balance at Beginning of Period	Additions at Cost	Deductions Charged to Cost and Expenses	Balance at Close of Period
1972	\$ —	\$ 149,342	\$ —	\$ 149,342
1973	149,342	1,017,476	(122,589)	1,044,229
1974	1,044,229	171,963	(653,826)	562,366

6. Commodore Systems, Inc.

In April 1972, Commodore Business Machines, Inc. entered into various agreements with Varadyne Industries, Inc., Bank of America, and others concerning Varadyne's calculator operations being conducted by its then subsidiary, Varadyne Systems, Inc. The name of this company was later changed to Commodore Systems, Inc. The arrangements provided, among other things, that Commodore Business Machines (Canada) Limited and subsidiaries would guarantee a bank line of credit for Commodore Systems, Inc. for up to \$1,000,000.

As of October 31, 1972, Commodore Systems, Inc. ceased to operate. The Company's obligation under the guaranteed line of credit was \$797,884 (Note 7) which has been reflected in the consolidated balance sheet as of June 30, 1973. In connection with its obligation under the line of credit, the Company received certain inventories and product research of Commodore Systems, Inc. After allocating the acquisition costs to assets received, the Company incurred a loss of \$112,000 which is included in cost of sales in the consolidated statement of operations in 1973.

7. Notes Payable to Banks and Others, Advances From Finance Company, and Mortgage Payable

Notes Payable to Banks and Others

The notes payable at June 30, 1974 and 1973 are described below:

	1974	1973
14% note payable, secured by a collateral mortgage on land owned by companies which are controlled by a director and also by the Chairman of the Board, due April 1975	\$1,000,000	\$1,000,000
15% note payable to the Company's Chairman of the Board, unsecured, due on demand	200,000	500,000
9½% note payable to a bank under the guarantee for Commodore Systems, Inc., secured by certain receivables and inventories, due in varying amounts through February, 1974	—	797,884
10% note payable to Diversified Credit Corporation (a Bahamian corporation owned by the Company's Chairman of the Board), unsecured, due on demand ...	17,500	50,000
12½%-12¾% notes payable to a bank, unsecured, due on various dates from July 11, 1974 to September 24, 1974	250,000	—
11% note payable by C.E.S.L. to a bank, secured by certain accounts receivable due on September 30, 1974	56,534	—
10¼% note payable by C.E.S.L. to a bank, secured by certain accounts receivable, due on July 6, 1974	40,633	—
17½% note payable by C.E.S.L. to a bank, secured by certain accounts receivable due on July 30, 1974	774,114	—
Revolving credit line with a bank with interest at 2% over existing prime rate, payable on demand, unsecured	667,393	—
Revolving credit line with a bank with interest at 2½% over existing prime rate, payable by and secured by documents of letters of credit	105,058	—
Current portion of mortgage payable	7,975	—
Total	\$3,119,207	\$2,347,884

During the year the Company's President loaned a subsidiary company \$50,000 on a non-interest demand note. The loan was repaid during the year.

During fiscal 1974 the highest balance owing to banks was \$1,960,000, the average balance owing to banks was \$1,233,000 and the average interest rate was 14½%.

The Company has compensating balance arrangements in connection with borrowings from four banks at June 30, 1974 as follows:

Compensating Balance Requirement	Compensating Balance Amount	Outstanding Loans at June 30, 1974	Accounts Receivable Discounted At June 30, 1974
			(Note 9)
\$50,000	\$25,000	\$250,000	\$ —
40,633	40,633	—	557,726
18,815	18,815	—	420,564
6,978	6,978	40,633	—

Advances from Finance Company

The Company has an agreement with a finance company whereby the Company may borrow on certain receivables and inventories, with interest at 4% over the prime rate in effect. During the fiscal year ending June 30, 1974, the highest balance owing was \$5,876,100, the average balance owing was \$4,683,700 with an average interest rate during the year of 13%.

Mortgage Payable

During fiscal 1974 the Company borrowed \$615,000 to finance the acquisition of a building and improvements. The mortgage balance at June 30, 1974, of \$601,472 is repayable over 25 years with interest at 8½%. The loan is secured by a deed of trust on the building.

8. Stock Options and Share Purchase Warrants

As of June 30, 1974, the Company has reserved 502,975 shares of common stock for exercise of stock options and share purchase warrants as follows:

Employee Stock Option Plan—The Company had reserved 64,000 shares of common stock for issuance to key employees under the Employee Stock Option Plan. In February 1974, 41,500 shares of this plan were cancelled and the Board of Directors approved (subject to shareholder approval) a new stock option plan, designed to qualify under Section 422 of the Internal Revenue Code. Under the plan, options to purchase up to 150,000 shares of the Company's common stock may be granted to certain key employees at not less than 100% of the fair market value of the shares at the date of grant. The options are exercisable in cumulative annual increments of 33 percent after the first nine months and expire five years from date of grant. Cancelled options become available for future grant.

The following table summarizes options outstanding at June 30, 1974, and the number of options exercised under the plans during the two years ended June 30, 1974 (amounts are in Canadian dollars).

	Number Of Shares	Option Price	
		Per Share	Total
Options outstanding at June 30, 1974 were granted during-			
1971 (old plan)	12,500*	\$3.25	\$ 40,625
1974 (new plan)	19,000	6.69	127,110
Total	31,500		\$167,735
Options exercised during-			
1973 (old plan)	13,266	\$3.25 to 6.97	\$52,288
1974 (old plan)	10,000	3.25	32,500

*These options may be exercised until November 1980.

There were no options which became exercisable during 1974. Between July, 1973 and February, 1974, under the old plan, there were 15,000 shares granted and 38,000 shares cancelled. There were 18,500 shares (old plan) as of June 30, 1973 and 131,000 shares (new plan) as of June 30, 1974 available for grant. As of June 30, 1974, only the options for 12,500 shares under the old plan were exercisable.

Proceeds from the sale of common stock upon exercise of options are credited to the common stock account. No charges or credits are made to income in connection with stock option transactions.

Share Purchase Warrants—At June 30, 1974, the Company has reserved 340,475 shares of common stock for exercise of the outstanding Share Purchase Warrants. The Share Purchase Warrants entitle the holders thereof to purchase an equal number of fully-paid, non-assessable shares of common stock at the exercise price on or before the date at which the warrants become void.

Series of Share Purchase Warrants	Date from Which Warrants are Exercisable	Expiration Date of Warrants	Price (Canadian dollars) at Which Warrants are Exercisable	Number Out- standing June 30, 1974
Series "A"	July 1, 1963	Nov. 1, 1974	\$4.50	194,975
Series "B"	July 1, 1963	May 1, 1975	\$5.50	51,000
Series "C"	June 1, 1964	April 1, 1976	\$5.50	94,500
				<u>340,475</u>

9. Commitments and Contingent Liabilities

At June 30, 1974, some of the premises utilized by the Company and its subsidiaries were occupied under long-term leases which expire at various dates to 1993. Annual rentals were \$373,500 in 1974 and \$150,000 in 1973. Aggregate minimum rental commitments remaining under these lease contracts after June 30, 1974, are as follows:

Fiscal Year Ending June 30,	Amount
1975	\$ 386,476
1976	355,276
1977	321,582
1978	255,420
1979	255,572
1980-1993	846,764
Total remaining obligations as of June 30, 1974	<u>\$2,421,090</u>

The Company also has a purchase option on a building located in England exercisable not less than 90 days before the expiration of any of the three years of the lease term at an option price decreasing from \$515,000 in the first year to \$450,000 in the third year.

As of June 30, 1974, the Company has purchase commitments of approximately \$7,600,000 which are cancellable under certain conditions, for future delivery of component parts and for assembly of calculators.

The Company is contingently liable at June 30, 1974, for trade receivables of approximately \$1,124,728 discounted at banks.

The Company has guaranteed a bank loan of approximately \$1,000,000 for Commodore France, S.A., a joint venture.

10. Litigation

A number of legal actions have been brought against the Company and/or its subsidiaries primarily by certain suppliers. The actions brought by the suppliers generally allege breach of contract relating to component parts or assembly of calculators which the Company has found to be defective or not suitable, and has either returned to the supplier or withheld payment or both.

In one action, a supplier is seeking damages in excess of \$600,000 relating to component parts delivered to the Company and subsequently returned to the supplier as being defective. The Company has filed a cross-complaint to this action seeking damages of \$3,000,000. In another action, a supplier alleges breach of contract, fraud and misrepresentation and seeks actual and punitive damages aggregating \$1,772,000. Component parts purchased from this supplier were found by the Company not to meet required specifications, and accordingly the parts were rejected. In still another action, a supplier alleges loss of profits and other damages aggregating approximately \$3,500,000. The Company has counterclaimed against this supplier alleging breach of contract and other charges.

Other actions in which the Company is involved are relatively less material than those described above. Based upon the opinions of counsel, management believes that the ultimate settlement of all currently pending legal actions will not have a material effect upon the Company's financial position or results of operations.

11. Earnings Per Share Canadian Method—Primary earnings per share are based upon the weighted average number of shares outstanding during each year. Fully diluted earnings per share have been calculated by assuming that the proceeds from the exercise of stock options and warrants have been applied first to reflect a reduction in the borrowing costs incurred by the Company, then to the purchase of short-term marketable securities at a yield of 4½ percent per annum. This results in an increase in net income of approximately \$121,000 in 1974 and \$95,000 in 1973 for purposes of this calculation.

The average number of shares used in calculating earnings per share was as follows:

	<u>1974</u>	<u>1973</u>
Weighted average common shares outstanding during the years	1,268,110	1,252,535
Effect of assumed exercise of stock options and warrants	373,683	396,412
Total common shares, assuming full dilution	<u>1,641,793</u>	<u>1,648,947</u>

United States Method—Earnings per share have been computed by dividing net income by the weighted average number of common shares and common share equivalents outstanding during each period. In 1974, net income was assumed to be increased by \$22,566 from the application of the proceeds from assumed exercise of options and warrants for purposes of the computation. Common shares and common share equivalents included in these computations are summarized in the following tabulation:

	<u>1974</u>	<u>1973</u>
Weighted average common shares outstanding during the years	1,268,110	1,252,535
Effect of assumed exercise of dilutive stock options and warrants	140,434	261,441
Total common shares and common share equivalents	1,408,544	1,513,976
Assumed additional common shares from exercise of dilutive stock options and warrants resulting from use of market price of common stock at end of year	—	2,022
Total common shares, assuming full dilution	<u>1,408,544</u>	<u>1,515,998</u>

12. Fourth Quarter Results of Operations—Sales during the three months ended June 30, 1974 were approximately \$13,300,000. However, a change in the method of recognizing certain sales and cost of sales was made in the fourth quarter; if the change had been made as of March 31, 1974, sales for the nine months would have been reduced by approximately \$5,100,000 with no significant effect upon gross profit.

The results of operations in the fourth quarter were adversely affected by year-end adjustments totalling \$2,900,000 (before tax effect) primarily related to inventory write-downs and accounts receivable credits.

13. Remuneration of Directors and Senior Officers

Aggregate direct remuneration paid or payable by the Company and its subsidiaries for the year to directors and senior officers of the parent company was approximately \$225,000.

Auditors' Report

To the Shareholders of

Commodore Business Machines (Canada) Limited:

We have examined the consolidated balance sheets of Commodore Business Machines (Canada) Limited (an Ontario corporation) and subsidiaries as of June 30, 1974 and 1973, and the related consolidated statements of operations, shareholders' equity and changes in financial position for the years then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the consolidated financial statements referred to above present fairly the consolidated financial position of Commodore Business Machines (Canada) Limited and subsidiaries as of June 30, 1974 and 1973, and the results of their operations and the changes in their financial position for the years then ended, in conformity with generally accepted accounting principles consistently applied during the periods.

ARTHUR ANDERSEN & CO.

San Jose, California,
September 27, 1974.

Board of Directors	Irving Gould Coral Harbour, N.P., Bahamas	Head Office	946 Warden Avenue Scarborough, Ontario
	Jack Tramiel Saratoga, California	Executive Office	901 California Avenue Palo Alto, California 94304
	Vincent Paul Toronto, Ontario		
	Burton Winberg Toronto, Ontario	Other Offices	Commodore Business Machines, Inc. 901 California Avenue Palo Alto, California 94304
	Henry B. Sussman Toronto, Ontario		2890 Lee Highway Bristol, Virginia 24201
Officers	Irving Gould Chairman of the Board		Commodore International Limited P.O. Box 4852, Bolam House Nassau, Bahamas
	Jack Tramiel President		CBM Business Machines, Limited 446 Bath Road Slough SL1 6BB, England
	Gerald van Buskirk Vice-President		Eaglescliffe Industrial Estate Eaglescliffe, Stockton on Tees Teeside TS 160 PN, England
	Samuel Bernstein Vice-President		Commodore Buromaschinen GmbH Am Schafbrinke 62c 3000 Hannover 17 West Germany
	Eugene Stewart Vice-President		Commodore France S.A. 39 rue Victor Masse 75009 Paris, France
	Gerald Worth Secretary-Treasurer		Commodore Japan Limited Taisei-Denshi Building 8-14 Ikue 1-Chome Asahi-Ku, Osaka 535
Transfer Agent and Registrar	Canada Permanent Trust Company Toronto, Montreal		Commodore Switzerland S.A. Bahnhofstrasse 74 CH 5000 Aarau, Switzerland
Auditors	Arthur Andersen & Co. San Jose, California		Commodore Educational Systems Limited P.O. Box N8312 Bolam House Nassau, Bahamas
Counsel	Davies, Ward & Beck Toronto, Ontario		Brunswick Building 5-27-7 Sendaguya Shibuya-Ku, Tokyo, Japan
Shares Listed	American Stock Exchange Canadian Stock Exchange Montreal		



**Commodore Business Machines
(Canada) Limited**